



Members of the Board of Retirement

James A. Diepenbrock, President
Appointed by the Board of Supervisors

John B. Kelly, Vice President
Appointed by the Board of Supervisors

Michael DeBord
Elected by the Retired Members

Keith DeVore
Appointed by the Board of Supervisors

Richard B. Fowler II
Appointed by the Board of Supervisors

Diana Gin
Elected by the Miscellaneous Members

Kathy O'Neil
Elected by the Miscellaneous Members

Chris A. Pittman
Elected by the Safety Members

Julie Valverde
Ex Officio, Director of Finance

John Conneally
Elected by the Safety Members

Martha J. Hoover
Elected by the Retired Members

Executive Staff:

Richard Stensrud
Chief Executive Officer

Scott Chan
Chief Investment Officer

Robert L. Gaumer
General Counsel

Kathryn T. Regalia
Chief Operations Officer

John W. Gobel, Sr.
Chief Benefits Officer

MINUTES

RETIREMENT BOARD MEETING, WEDNESDAY, JUNE 18, 2014

A regular meeting of the Retirement Board was held in the Sacramento County Employees' Retirement System Administrative Office, 980 9th Street, 19th Floor, Sacramento, California, on Wednesday, June 18, 2014, and commenced at 10:04 a.m.

OPEN SESSION:

PUBLIC COMMENT:

1. None heard.

MINUTES:

2. The Minutes of the May 22, 2014 special meeting were approved on Motion by Ms. Valverde; Seconded by Mr. DeVore. Motion carried (8-0).

CONSENT MATTERS:

Items 3-7

The Consent Matters were acted upon as one unit upon a Motion by Mr. Fowler; Seconded by Ms. Valverde. Motion carried (8-0).

3. CHANDLER, Jayne L.: Denied a service-connected disability retirement.

CONSENT MATTERS (continued):

4. WEIR, Shannon D.: Granted a service-connected disability retirement.
5. Approved the proposed interest crediting rate for member contribution accounts for the six month period ending June 30, 2014.
6. Approved proposed extension of the agreement with Segal Consulting to provide actuarial services.
7. Received and filed the May 2014 Monthly Investment Manager Compliance Report and Watch List.

ADMINISTRATIVE MATTERS:

8. Chief Executive Officer Richard Stensrud provided an update on developments affecting public retirement systems and on miscellaneous system and staff activities.

Mr. Stensrud reported that for the 15th consecutive year, SCERS has earned the Government Finance Officers Association (GFOA) Certificate of Achievement for Excellence in Financial Reporting for their comprehensive annual financial report. Mr. Stensrud commended the Staff on their accomplishment.

Mr. Stensrud reported on legislation being brought forward by the State Association of County Retirement Systems (SACRS). Mr. Stensrud stated that AB 2473, which would bring the 1937 Act into conformity with federal tax laws, and AB 2474, which would integrate the 1937 Act with PEPRA, were both progressing through the legislature. Mr. Stensrud reported that after a pension reform conference, questions were raised regarding the 1937 Act treatment of 'excess earnings.' Mr. Stensrud stated that this prompted discussion when AB 2473 was heard in the Senate committee, but that SACRS explained to the committee that AB 2473 had no impact on the provisions in question other than to make them compliant with federal tax law and a unanimous vote was reached to move the bill forward.

Mr. Stensrud noted that legislation was also progressing that would apply an education requirement similar to that imposed on 1937 Act retirement system boards to the CalPERS board.

Mr. Stensrud reported that for the first time in several years, SCERS is expected to have unallocated earnings at the end of the fiscal year, approximately \$70 million. Mr. Stensrud stated that SCERS' standard procedure is to take half of the unallocated earnings and place it in the contingency reserve and to apply the other half toward the existing unfunded liability. Mr. Stensrud noted that the Board would take formal action on the application of the unallocated earnings in the Fall.

ADMINISTRATIVE MATTERS (continued):

Mr. Stensrud reported that he is continuing to meet with SCERS' stakeholders to discuss SCERS' strategic plan for 2014-2018. Mr. Stensrud noted that the strategic plan has been well received.

Mr. Stensrud stated that changes would be made to the manner in which Staff addresses the quarterly investment reports prepared by the investment consultants. Mr. Stensrud explained that going forward, rather than simply reporting on investment performance, Staff would focus on explaining the investment performance in the context of the asset allocation and the portfolio structure as a whole. Mr. Stensrud said that the goal was to provide a strategic level analysis and discussion of how the construction of the investment portfolio impacts investment performance, as well as considerations in positioning the portfolio to optimally respond to future market developments.

Mr. Stensrud reported that for the same purpose of maintaining a focus on the strategic elements of the investment program, in the future special Board meetings would be held with the sole focus on investments. Mr. Stensrud stated that these meetings might include presentations from investment managers, panel discussions, and more in-depth review of investment topics.

Mr. Stensrud reported on the Ventura County pension reform ballot initiative. Mr. Stensrud noted that the Ventura County Counsel had recently issued a legal opinion on the ballot initiative. Mr. Stensrud and General Counsel Robert Gaumer stated that the opinion determined that the initiative was unlawful and invalid on multiple fronts. Mr. Stensrud also noted that the initiative would dissolve the retirement board and system, and therefore there would be no entity in place to manage the plan's assets. Mr. Stensrud noted that it was unclear whether a court decision on the initiative could be obtained before the vote was held on the initiative. Discussion followed.

9. Chief Operations Officer Kathy Regalia presented the proposed SCERS administrative budget for the 2014-2015 fiscal year. Ms. Regalia stated that the proposed budget was only nominally higher than last year's budget, and at 0.07% of actuarial accrued liabilities, was well below the 0.21% cap imposed by the 1937 Act. Ms. Regalia further stated that the biggest change was due to County approved cost of living increases to some of the Staff, offset somewhat by those Staff members contributing more toward their retirement benefits. Ms. Regalia noted that the County was continuing to negotiate with certain bargaining units and that changes may need to be made to the final budget to reflect those negotiations. Discussion followed.

Motion by Ms. Gin to approve the proposed SCERS administrative budget for the 2014-2015 fiscal year; Seconded by Mr. DeVore. Motion carried (8-0).

ADMINISTRATIVE MATTERS (continued):

10. Chief Executive Officer Richard Stensrud introduced Paul Angelo and Andy Yeung of Segal Consulting who provided an educational presentation on the new financial reporting rules adopted by the Governmental Accounting Standards Board (GASB) for retirement systems and participating employers reports (GASB Statements 67 and 68).

Mr. Angelo stated that GASB Statement 67 is the standard that applies to the financial reports of the retirement system and replaces GASB Statement 25. Mr. Angelo also stated that GASB Statement 68 is the standard that applies to the financial reports for the employer and replaces GASB Statement 27.

Mr. Angelo reviewed the four significant changes in the new rules, including: (1) Placing the net pension liability into a more prominent location on the balance sheet for the employers rather than in the required supplementary information; (2) Decoupling expense from funding; (3) Accounting for cost-sharing plans; and (4) Expanding disclosure information (notes and required supplementary information).

Mr. Angelo noted that under the new GASB rules, for plans like SCERS that receive the annual required contribution (ARC) pursuant to a written actuarial funding policy, for funding purposes the discount rate on the liabilities would continue to be the long term investment return assumption. Mr. Angelo noted, however, that the new GASB rules did impact how the discount rate is reported in the employer's financial statements, specifically, that it must be net of investment expenses, but not net of the retirement system's administrative expenses as had previously been the case. Mr. Angelo discussed the complications associated with this change. Mr. Angelo also discussed how employers in pooled plans (like SCERS) will now have to recognize and report a proportionate share of the pool's liabilities and expenses.

Mr. Angelo discussed the timing and frequency involved in GASB Statements 67 and 68. Mr. Angelo noted that for Statement 67, the net pension liability measurement date must be as of the pension plan's most recent fiscal year-end, while for Statement 68, the net pension liability measurement date can be earlier than the fiscal year-end reporting date but not earlier than the end of the prior fiscal year.

Discussion followed.

Motion by Mr. Fowler to receive and file the educational presentation on the new financial reporting rules adopted by the Governmental Accounting Standards Board (GASB) for retirement systems and participating employers reports (GASB Statements 67 and 68).; Seconded by Ms. Valverde. Motion carried (8-0).

ADMINISTRATIVE MATTERS (continued):

11. Paul Angelo and Andy Yeung of Segal Consulting presented the actuarial experience study for the period July 1, 2010 through June 30, 2013 and the review of economic actuarial assumptions for the June 30, 2014 actuarial valuation.

Mr. Angelo noted that pursuant to SCERS' policy, the actuarial experience study is performed every three years, and while the review of economic actuarial assumptions can be performed more frequently, the practice is to perform it on the same cycle as the experience study.

Mr. Angelo and Mr. Yeung reviewed the actuarial assumption changes recommended by Segal based on the actuarial experience study. Mr. Yeung noted that Segal made recommendations to: (1) Adjust retirement rates to reflect slightly later retirements for members; (2) Adjust the retirement rates to reflect slight mortality improvement; (3) Adjust termination rates to reflect lower incidence of termination overall; (4) Adjust disability rates to reflect slightly lower incidence of disability; (5) Use years of service instead of age in determining and applying the merit and promotional rates of salary increase; and (6) Maintain the current assumption to anticipate conversion of unused sick leave at retirement. Mr. Yeung noted that the net impact of the various assumption changes was a small reduction in the normal cost. Discussion followed.

Motion by Ms. Valverde to receive and file the actuarial experience study and to adopt the actuarial assumptions recommended in the report; Seconded by Mr. Fowler. Motion carried (8-0).

Mr. Angelo and Mr. Yeung reviewed the changes recommended by Segal based on the review of economic actuarial assumptions. Mr. Angelo stated that Segal is recommending to: (1) Maintain the assumed rate of price inflation at 3.25% annually; (2) Maintain the current investment return assumption of 7.50% annually; (3) Maintain the current inflationary salary increase assumption of 3.25%; and (4) Maintain the current real "across the board" salary increase assumption of 0.25%.

Mr. Angelo described the methodology Segal uses in determining the investment return assumption.

Mr. Angelo explained that Segal determines the projected real rate of return for the next 10-15 years (an approximation of the duration of the fund's liabilities) by taking SCERS' asset allocation model and plugging in the various asset class return projections from SCERS' general investment consultant, Strategic Investment Solutions, and the investment consultants advising eight other California public retirement systems. In determining SCERS' specific real rate of return, Segal then uses the average of the expected real rates of return as it reflects a broader range of capital market information. Mr. Angelo noted that the real rate of return in the current study is slightly lower (0.30%) than the projected real rate of return used in the last review of economic assumptions.

ADMINISTRATIVE MATTERS (continued):

Mr. Angelo explained that Segal then adjusts the real rate of return to reflect the potential risk of shortfall in the returns analysis. Segal does this by taking the variability of returns for the various asset classes (i.e., the standard deviation, which is 0.07% higher than in the last review of economic assumptions) and applying a risk adjustment to increase the likelihood of achieving the investment return assumption over a 10-15 year period. Segal presents the result in the form of a 'confidence level' that the actual average return will equal or exceed the investment return assumption over the extended period.

Mr. Angelo noted that given the slightly lower real rate of return projections and the slightly higher portfolio standard deviation, the 7.50% investment return assumption reflects a confidence level of 60%, which is 4% lower than the confidence level for the 7.50% return assumption in the last review of economic assumptions. Mr. Angelo further noted that the 60% confidence level is still on the higher end of the 50%-60% range utilized by most of Segal's California public retirement system clients. Mr. Angelo also noted that since both the projected real rate of return and standard deviation numbers are based on assumptions about future events, the confidence level is a relative rather than absolute measure.

Mr. Angelo discussed the options and ramifications with respect to the GASB rule change requiring that the employer's financial statement utilize an investment return assumption determined net of investment expenses but not net of administrative expenses.

Mr. Angelo stated that currently the investment return assumption is net of all costs, investment and administrative. Accordingly, maintaining the current practice could result in two slightly different investment return assumptions – i.e., one for funding purposes and one for financial reporting by the employer. Mr. Angelo noted that GASB does not require that the investment return assumption for funding be the same as for employer financial reporting, but Mr. Angelo noted the value in not having discrepancies between the investment return assumptions. Mr. Angelo further noted, however, that if SCERS were to continue to develop the investment return assumption net of both investment and administrative expenses in the upcoming actuarial valuation, there would not be a discrepancy between the investment return assumption for funding and employer financial reporting purposes.

Mr. Angelo explained that if SCERS were to modify its method of calculating the investment return assumption to make it net of only investment cost, it would require a new breakdown of normal cost in the actuarial valuation to include a percentage of pay allocation for administrative expenses. It would also require a determination of how to allocate that cost between employers and members. Mr. Angelo noted that this could be a source of confusion and disagreement between members and participating employers.

Mr. Angelo stated that while Segal believed that a uniform investment return assumption for both funding and employer financial reporting is ultimately the best practice, given these considerations, Segal believed that both options for determining the investment return assumption were reasonable.

ADMINISTRATIVE MATTERS (continued):

Mr. Stensrud stated that Staff recommended maintaining the current method for calculating the investment return assumption. Mr. Stensrud noted that in the upcoming valuation there would be no difference between the investment return assumption used for funding versus that used for reporting. Accordingly, there would be no detriment to participating employers with respect to financial reporting under the new GASB rules. Mr. Stensrud noted that conversely, the complications of changing the method of calculating the investment return assumption were real and material. Mr. Stensrud stated that the costs of the system have been and will continue to be fully disclosed and fully addressed under the current methodology. Mr. Stensrud further noted that the allocation of the costs will remain the same. Finally, Mr. Stensrud noted that Staff agrees that changing the method of calculating the investment return assumption to remove discrepancies should be made at some point, but that it was not necessary to do so now.

Discussion followed.

Motion by Mr. DeVore to approve Staff's recommendation to maintain the economic actuarial assumptions and the current method for calculating the investment return assumption; Seconded by Ms. Hoover. Motion carried (8-0).

12. General Counsel Robert Gaumer presented the proposed materials for providing education and oversight regarding post-retirement employment of SCERS' retirees by employees participating in SCERS. Discussion followed.

Motion by Ms. Valverde to approved the proposed materials for providing education and oversight regarding post-retirement employment of SCERS' retirees by employees participating in SCERS; Seconded by Mr. Pittman. Motion carried (8-0).

INVESTMENT MATTERS:

13. Jamie Feidler of Cliffwater, LLC presented the Alternative Assets Investment Performance Report for periods ending December 31, 2013 and March 31, 2014, including information regarding the hedge fund, private equity, real assets, and opportunities portfolios.

Mr. Feidler reported that SCERS' hedge fund portfolio was up 1.2% in the first quarter of 2014, in-line with the absolute policy benchmark (90-day T-Bills + 5%) which was up 1.2%. Mr. Feidler noted that SCERS' hedge funds outperformed the HFRI Equity Hedge Index in the first quarter of 2014, which was up 0.5%.

Mr. Feidler stated that the SC Absolute Return Fund, LLC ("SCARF") was up 1.4% in the quarter, and outperformed the HFRI Fund of Funds Composite Index and the 90-day T-Bills + 5%, which were up 0.5% and 1.2% respectively.

INVESTMENT MATTERS (continued):

Mr. Feidler stated that for the quarter, SCARF B returned 1.0%, which underperformed both SCARF and the 90-day T-Bills +5%, but outperformed the HFRI Fund of Funds Composite Index.

Mr. Feidler reported that SCERS' direct hedge fund program was up 1.2% during the first quarter, which again was in-line with the 90-day T-Bills + 5%, but outperformed the HFRI Fund of Funds Composite Index benchmark.

Mr. Feidler stated that second quarter to date, through May 31, 2014, SCERS' total hedge fund program is up 0.5%, the direct hedge fund program is up 0.4%, SCARF is up 0.4% and SCARF B is up 0.7%. These numbers compare to the HFRI Fund of Funds Composite Index and the 90-day T-Bills +5%, which are up 0.4% and 0.8%, respectively

Mr. Feidler reported that the net investment rate of return ("IRR") of SCERS' private equity portfolio was up 8.5% since inception compared to the Venture Economics Private Equity Index up 9.1% and the multiple of total value to paid in capital ("TVPI") is 1.17x since inception. Mr. Feidler noted that SCERS' private equity portfolio shows lower relative returns due to the early phase/cycle of investments (j-curve affect) compared to the index.

Mr. Feidler reported that, through December 31, 2013, SCERS' real assets portfolio IRR was 6.7% compared to SCERS' real assets portfolio benchmark (CPI + 5%) IRR of 7.3% and SCERS' TVPI was 1.2x.

Mr. Feidler reported that SCERS' opportunistic portfolio generated a net IRR of 8.5% as of December 31, 2013 which has outperformed SCERS' long-term benchmark (SCERS' actuarial rate of return) of 7.5%. In addition, SCERS' opportunistic portfolio has outperformed SCERS' intermediate benchmark with a return of 14.1% over the past three years compared to a 7.4% IRR for SCERS' policy benchmark.

Motion by Ms. Gin to receive and file the quarterly performance report; Seconded by Mr. Fowler. Motion carried (8-0).

14. Jennifer Young of The Townsend Group presented the quarterly performance report on real estate investments for the quarter ended March 31, 2014.

Ms. Young reported that SCERS' total real estate portfolio returned 3.1% during the first quarter of 2014, outperforming the benchmark (NFI-ODCE) of 2.3%. Ms. Young stated that for the 12-month period ending March 31, 2014, SCERS' real estate portfolio return was 10.6% and that in the same period, the benchmark returned 12.7%.

INVESTMENT MATTERS (continued):

Ms. Young reported that SCERS' domestic public REIT portfolio returned 10.4%, compared to a first quarter return of 8.5% for the FTSE NAREIT (domestic) REIT Index. Ms. Young stated that SCERS' international REIT portfolio returned -1.8% compared to a first quarter return of -1.2% for the FTSE EPRA/NAREIT Global ex-US REIT Index.

Ms. Young reported that SCERS' core real estate portfolio returned 2.4% during the first quarter, slightly outperforming the benchmark of 2.3%. Ms. Young stated that for the 12-month period ending March 31, 2014, SCERS' core real estate portfolio return was 10.4% and that in the same period, the benchmark returned 12.7%. Ms. Young further stated that both the core separate accounts and the core commingled fund returned 10.4% for the quarter.

Ms. Young reported that SCERS' non-core real estate portfolio returned 5.8% for the quarter, beating Townsend's benchmark of the NCREIF / Townsend Value Added Funds, which returned 2.6%. Ms. Young stated however that SCERS' non-core real estate portfolio returned 15.7% for the 12-month period, exceeding the benchmark return of 12.2%.

Motion by Mr. DeVore to receive and file the quarterly performance report; Seconded by Mr. Gin. Motion carried (8-0).

15. Chief Executive Officer Richard Stensrud introduced a discussion regarding the process for engaging in and modifying investment manager relationships in the equity and fixed income asset class components of SCERS' investment portfolio. Mr. Stensrud noted that the topic was being discussed because Staff would soon be bringing proposed Investment Policy Statements for the equity and fixed income asset classes to the Board, and the implementation protocol for those asset classes would need to be addressed.

Mr. Stensrud reviewed the current process used for the equity and fixed income asset classes and compared it to the implementation process used in the alternative asset classes. Mr. Stensrud noted that the primary difference was that in the equity and fixed income asset classes the Board made a final, formal decision on engaging or terminating an investment manager, while in the alternative asset classes those decisions had been vested in Staff and the consultants. Mr. Stensrud stated that going forward with the equity and fixed income asset classes, the current process could be maintained or it could be modified to an approach similar to that used with the alternative assets. Mr. Stensrud noted some advantages to using an approach similar to the alternative asset classes, but stated that Staff did not believe that changing the current equity and fixed income implementation protocol was necessary, only optional.

Discussion followed, including consideration of the mandate size in equity and fixed income versus the alternative assets, and the different timing considerations applicable to the different asset classes. Given the discussion, Mr. Stensrud stated that Staff would proceed

INVESTMENT MATTERS (continued):

with updating the investment policy statements for the equity and fixed income asset classes using the same implementation process as in the past. No action was requested or taken.

The meeting was adjourned at 2:15 p.m.

MEMBERS PRESENT: James A. Diepenbrock, Keith DeVore, Richard B. Fowler II, Diana Gin, Chris A. Pittman, Julie Valverde, John Conneally, and Martha J. Hoover.

MEMBERS ABSENT: John B. Kelly, Michael DeBord, and Kathy O’Neil.

OTHERS PRESENT: Richard Stensrud, Chief Executive Officer; Scott Chan, Chief Investment Officer; Robert L. Gaumer, General Counsel; Kathryn T. Regalia, Chief Operations Officer; John W. Gobel, Sr., Chief Benefits Officer; Steve Davis, Deputy Chief Investment Officer; Suzanne Likarich, Retirement Services Manager; Thuyet Dang, Accounting Manager; JR Pearce, Investment Officer; John Lindley, IT Administrator; Patrick Thomas, Strategic Investment Solutions, Inc; Jamie Feidler, Cliffwater LLC; Jennifer Young, The Townsend Group; Paul Angelo and Andy Yeung, Segal Consulting; and Diana Ruiz, Deputy County Counsel.

Respectfully submitted,

Richard Stensrud
Chief Executive Officer and
Secretary of the Retirement Board

APPROVED: _____
James A. Diepenbrock, President

DATE: _____

cc: Retirement Board (11); Board of Supervisors (6); County Counsel; County Executive (2); Internal Services Agency (2); County Labor Relations; Employee Organizations (20); Sacramento County Retired Employees’ Association; SCERS Member Districts (10); Elected Officials (3); Superior Court of California, County of Sacramento; Amervest Company, Inc.; Mark Merin; John R. Descamp; and The Sacramento Bee.